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C O N F I D E N T I A L SECTION 01 OF 03 CARACAS 000869

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TREASURY FOR KLINGENSMITH AND NGRANT  
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TAGS: [EFIN](#) [VE](#)

SUBJECT: IMF AND WORLD BANK: SO LONG AND THANKS FOR THE  
MEMORIES

REF: A. CARACAS 667

[1](#)B. CARACAS 844

[1](#)C. CARACAS 854

Classified By: Economic Counselor Andrew N. Bowen for reasons 1.4(B) and (D).

[1](#)1. (SBU) SUMMARY: On April 30, President Chavez announced that Venezuela would withdraw from the IMF and World Bank. The announcement, which followed action taken in March by Venezuela to pay off the last of its IMF and World Bank debt and continued negotiations regarding a Bank of the South, tracks with Chavez' goals of eliminating neo-liberal Western influence in Venezuela. Coupled with a departure from the International Center for Settlements and Investment Disputes (ICSID), these decisions would remove Venezuela from most multilateral financial agreements and remove potential recourses for investors in international fora. A withdrawal from the IMF could trigger debt defaults on Venezuela's bonds depending on their terms and has already led a fall in bond prices, and an increase in the parallel market rate (an indicator of capital flight). PDVSA is also in "technical default" with its creditors after the OPEC production cuts and subsequent nationalization of the Strategic Associations.  
END SUMMARY.

[1](#)2. (SBU) In the midst of a pre-Day of the Worker celebration speech on April 30, Chavez announced that Venezuela would leave the IMF and World Bank (reftel C). While addressing Minister for People's Power of Finance (MPPF) Cabezas, Chavez directed him to "formalize the departure of Venezuela from the World Bank and International Monetary Fund and all of that...I want to sign the order tonight already and insist that they return to us that which is ours" (apparently referring to Venezuela's holdings based on its initial USD 15 million paid in capital contribution).

[1](#)3. (SBU) Chavez followed up his attacks on the IMF and World Bank during a speech on May 3, arguing, "why do we need the World Bank, why do we need the IMF, for nothing. We will create our own Bank of the South, not a small bank, nor a small fund, no, a big bank my friend, and we'll put our reserves there and look for financing from other countries, on other continents." Chavez also alleged that after his April 30 announcement, a White House spokesperson threatened Venezuela (referring to Dept. Spokesman McCormack).

14. (C) Under the International Bank for Reconstruction and Development (IBRD) and International Monetary Fund (IMF) Articles of Agreement, a country ceases to be a member upon receipt of a notice in writing from the member. By leaving these institutions, a country remains liable for direct obligations and for contingent liabilities as part of any loans or guarantees previously contracted. Venezuela has paid off its obligations (septel), though it is possible that some loan guarantees may be outstanding. Once its liabilities are met, the institutions repurchase the country's shares and pay out the proceeds.

15. (SBU) Venezuela has approximately USD 250 million owed to it by the IMF and is one of the larger contributors in the World Bank's "Mexican Chair," which includes Mexico, Venezuela, Spain, Costa Rica, Guatemala, and represents El Salvador, Honduras, and Nicaragua. The World Bank has 185 member countries and Venezuela has been a member of these institutions since 1946. Venezuela has a 1.22 percent share of the votes at the IMF. Venezuela's departure would put it in the company of such economic luminaries as Cuba and North Korea.

16. (SBU) During the ALBA summit in Barquisimeto on April 29, Evo Morales announced that all ALBA countries would withdraw from the International Center for Settlements and Investment Disputes (ICSID) (reftel B). Seeming to speak for all attendees, Morales stated, "the governments of Latin America and of the whole world never win the disputes, the transnationals always win...what is the (one) country that has won...? the United States..." Most large investments in Venezuela are protected by Bilateral Investment Treaties (BIT), the most popular being the Dutch, that provide an outlet to arbitration. Given the state of the judicial system in Venezuela, these clauses are considered essential to protect investments in Venezuela and post is aware that at

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least two of the four Strategic Associations are protected by such BITs.

17. (C) According to Venezuela's Alternate Director at the World Bank (and former Vice Minister of Finance) Jose Rojas (STRICTLY PROTECT THROUGHOUT), a departure from the IMF and World Bank would have severe negative consequences for the Venezuelan government and Venezu}Ez{Q8.r goods up front (rather than on delivery or on a 90-day basis. It would also significantly reduce Venezuelan companies and banks access to credit because there would be no guarantor of last resort. Rojas also believes that it would become impossible for Venezuela to issue new debt due to the lack of implicit IMF backing. Rojas also argues that Venezuela would lose its rights in most multilateral institutions such as the World Trade Organization as well as many of the rights afforded to it by bilateral accords. This means that Venezuela and Venezuelan companies could not defend themselves against unfair practices. (COMMENT: These are the views of an individual who is probably out of a job if Venezuela withdraws from the World Bank and may be overstating the consequences. Nevertheless, we have found Rojas to be a competent and reliable interlocutor. END COMMENT).

18. (SBU) Since the announcement on April 30, the country risk indicator (the yield gap between Venezuelan and U.S. bonds) increased fourteen basis points. Bloomberg reports that as much as USD 21 billion of the country's external debt includes clauses similar to those in its 9.375 percent bond maturing in 2034, which reads that "Venezuela ceasing to be a member of the IMF is an event of default." While withdrawal from the IMF would result in a technical default in this instance, it does not necessarily mean that creditors would call in their loans, or that Venezuela would stop its payments. The global glut of liquidity has led to a very forgiving lending environment and it would be hard for investors to find well-yielding instruments to place their

money to replace these loans. After Chavez' speech, Minister for People's Power of Finance (MPPF) Cabezas clarified on May 1 that, "The Bolivarian Republic of Venezuela is committed short, medium, and long term to paying its debt. Our problem isn't with bondholders, but with the International Monetary Fund."

¶9. (SBU) The ability of bondholders to demand accelerated payments in the event of a default could cost the BRV up to USD 4.5 billion according to Santander Investments. While Venezuela has approximately USD 27 billion in outstanding external debt, only USD 4.5 billion or so is trading below face value, meaning it can be purchased for less money than the Venezuelan government would owe the holder should they demand repayment. Venezuela could issue new debt to pay off this amount, but doing so could be costly given the rates it would have to pay on the new debt. Given that these bonds still offer decent yields, most analysts think that a demand for accelerated repayment at this point seems unlikely.

¶10. (SBU) At the same time, the value of the bolivar fell almost 3 percent in the parallel market to Bs. 3850/dollar during the past two days (the official rate is Bs. 2150/dollar). The bolivar's value has fallen over eight percent in the past month, despite the issuance of USD 7.5 billion in dollar-denominated debt by PDVSA (reftel A). The PDVSA bonds also fell in trading after May 1, which will hurt many investors who have held off on selling their bonds in the hopes that prices would go up after the initial issuance.

¶11. (SBU) These fluctuations were accompanied by the announcement by the consortium of bondholders for the Cerro Negro Strategic Association (SA) that OPEC production cuts and the change in ownership of the Association following the May 1 "nationalizations" (reftel C) constituted a prospective technical default. Cerro Negro has USD 500-600 million in outstanding bonds, which are serviced through oil sales by the Association. In an attempt to calm markets, PDVSA director Eulogio Del Pino stated on May 1 that PDVSA could pay off the SA debt, if necessary. This led to massive buying and selling in SA debt as people sold off debt trading above face value and bought up lower yielding, discounted

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debt. Estimates are that there are over USD 3 billion in outstanding bonds between the four SAs. (NOTE: Technically, all four SAs have been in default since they were forced to make OPEC cuts at the beginning of 2007. Though, this marks the first time that lenders have publicly commented on a threat to their loans. END NOTE).

¶12. (C) COMMENT: The televised nationalization of the SAs in the Faja on May 1st seems to have been overshadowed by the announcements regarding the World Bank and IMF on April 30. All signs are that the BRV intends to follow through with this withdrawal, although we understand no formal notification has been transmitted to either institution. By leaving these institutions, Venezuela will further isolate itself from the international community and international markets. Without either a "creditor of last resort" or impartial arbiter for commercial disputes, Venezuela will, in effect, eliminate the two remaining insurance policies that exist for investors in Venezuela. This will increase Venezuela's cost of financing and potentially hurt Venezuelan consumers who have to pay higher prices for goods. It will also mean that, in the event of a financial crisis, the remedy will be that much harsher. END COMMENT.

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